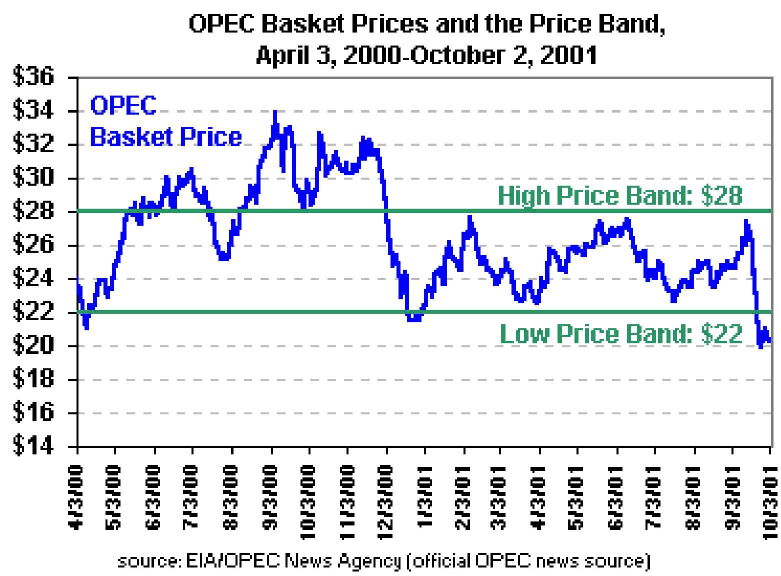
October 4, 2001

OPEC

Organization of Petroleum Exporting Countries (OPEC) members Algeria, Indonesia, Iran, Iraq, Kuwait, Libya, Nigeria, Qatar, Saudi Arabia, the United Arab Emirates, and Venezuela produce about 40% of the world's oil and hold more than 77% of the world's proven oil reserves. OPEC also contains most of the world's excess oil production capacity.

RECENT DEVELOPMENTS

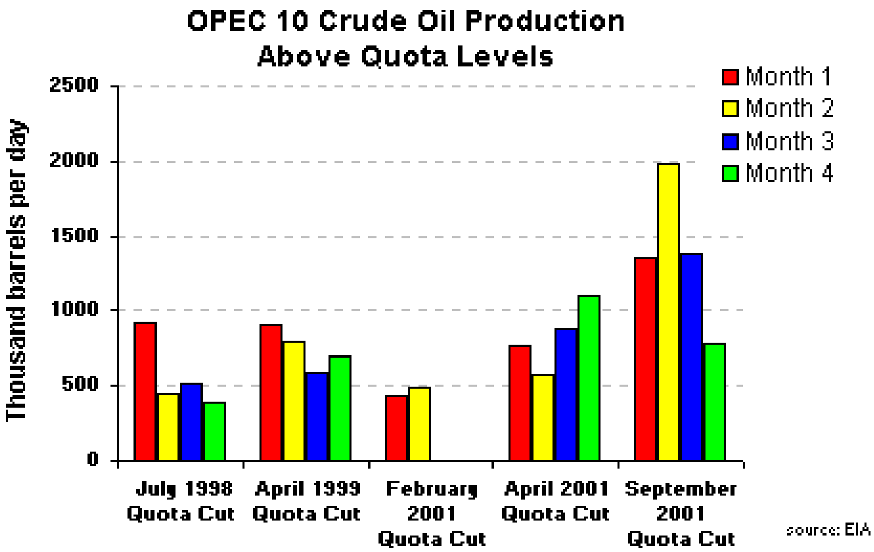
Oil prices collapsed on September 24, in the largest single day price drop since January 1991. The September 11 terrorists attacks inside the U.S. and the world economic downturn appear to have precipitated new OPEC flexibility regarding its $25 price target for its basket of crude oils. Two days after the oil price collapse, on September 26, OPEC held its already-scheduled meeting and refrained from altering production quotas, despite the basket price hovering near two-year lows.



During its March 2000 meetings, OPEC adopted an informal price band mechanism (formally ratified on January 17, 2001) whereby OPEC basket prices higher than $28 per barrel or lower than $22 per barrel would trigger automatic production adjustments. Prices sustained above the price band's target range for 20 trading days are to result in a *pro rata* production increase of 500,000 bbl/d, while prices below the target range for 10 trading days are to result in *pro rata* cuts of 500,000 bbl/d.

Kuwaiti Oil Minister Adel Al-Subeih has stated that the band is intended for use during "normal" periods, not times of volatile markets and economic uncertainties. Hence, it would not be appropriate to use the mechanism at the current time. EIA expects oil prices in 2002 that will keep the basket price near the low end of it price band.

In the 19-month history of the price band, the mechanism has seldom been used. In 397 days of trading, OPEC's basket price has closed above OPEC's upper $28 band 121 times and below the lower $22 band 16 times (through October 2). In decisions reached at OPEC meetings (and one decision reached during a conference call), OPEC has raised its quotas three times and reduced its quotas three times. Only one of these quota changes was the result of a price band activation.

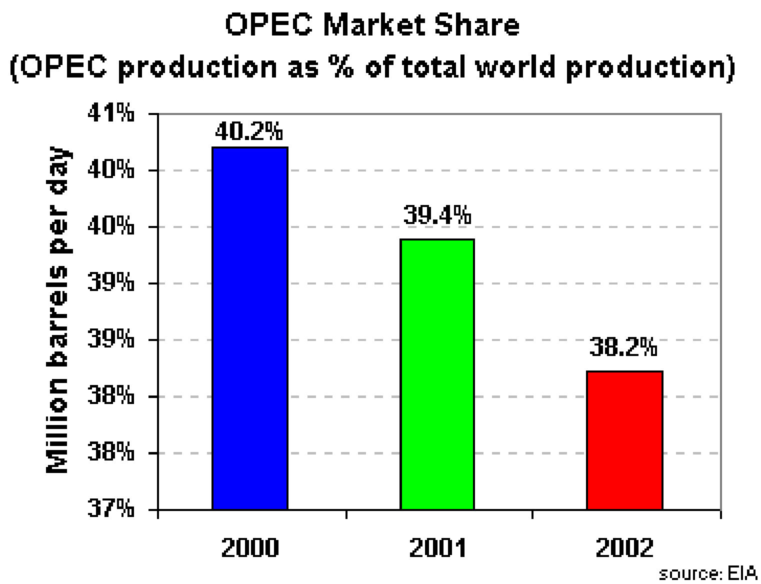


Graph shows the amount by which OPEC 10 production exceeded quotas for the four months following each of its recent quota reduction.

OPEC COMPLIANCE

Prior to September 11, EIA had not anticipated OPEC fulfilling its September 1, 1-million-bbl/d quota reduction. Events since that date have made it increasingly likely that OPEC production will greatly exceed its quota levels in the fourth quarter of 2001. Over-production is expected to spike in October, with production approaching February 2001 quota levels.

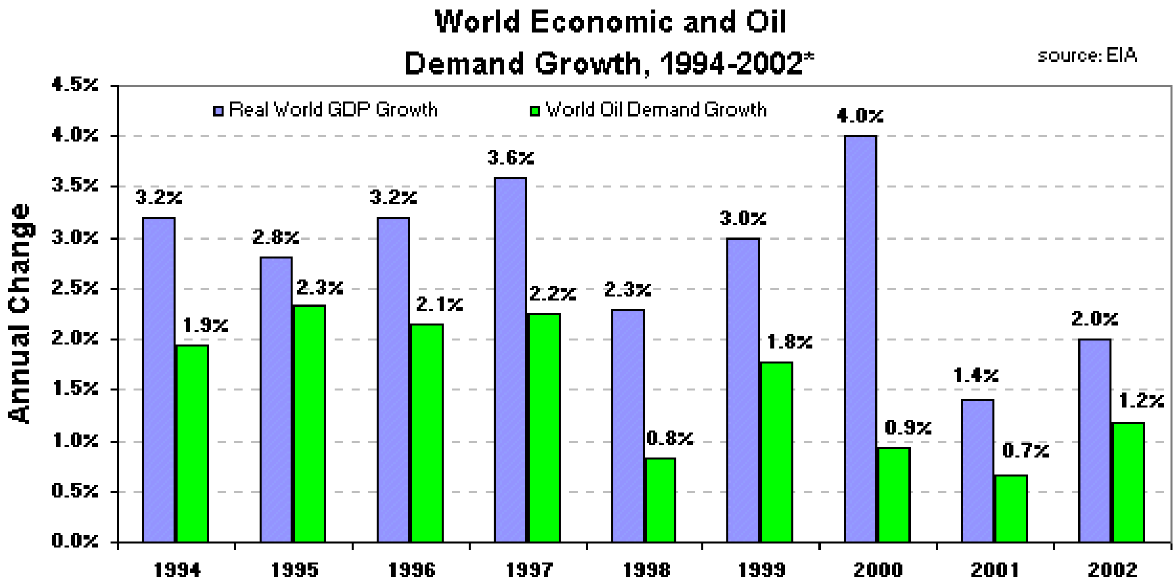
OPEC's unusually low quota compliance comes as members contemplate how to manage competing interests: OPEC's share of world oil markets and high oil prices. In the last year and a half, OPEC appears to have been defending price at the expense of market share, a situation that might be changing. Adding to OPEC's woes is the possibility that non-OPEC production in 2002 might outpace world demand growth.



World Oil Demand

In its previous Outlook, EIA noted that world oil demand during the past decade grew by at least 1 million barrels per day except during periods of serious international crises. A week after the release of the Outlook, the world did indeed enter a serious political and economic crisis, and moved closer to a global recession. In the near-term, the largest impact is expected to come from the large drop in global demand for jet fuel. Worldwide jet-fuel demand probably fell by about 10 percent outside the United States and by as much as twice that much within the United States. EIA's Outlook for 2002 assumes that following the initial stages of the crisis, commercial jet fuel use will recover somewhat, and that global jet fuel demand will be down by roughly 5 percent.

In addition, revised economic estimates indicate that the United States, viewed as the engine for global economic growth, may be in the midst of downturn. The events of September 11 have further weakened the world's economies, reducing oil demand further, leaving OPEC to supply a world oil market that is projected to be much smaller in 2002 than previously expected. Growth in world oil demand in 2002 is now estimated at 900,000 barrels per day, down from 1.4 million barrels per day in EIA's previous Outlook.



Graph demonstrates the imperfect relationship between economic and oil demand growth. In 1995, oil demand grew more than it had in 1994, even as economic growth was slower than in 1994. In 2000, economic growth was stronger than in 1999, but oil demand growth was weaker than in 1999.

*Please note that data for 2001 and 2002 are estimates.

In 2001, the OPEC 10 have been proactive in making production quota cuts in anticipation of market conditions that could weaken prices for their crude oils. They have been especially sensitive to weakening oil demand. However, the recent turmoil in world oil markets has left OPEC cautious about responding to the latest downturn in demand. Iranian Oil Minister Bijan Zanganeh stated that "the current situation is not because of the fundamentals in the market-- I believe there is no reason to panic." This sentiment was echoed by Saudi Arabian Oil Minister Ali Naimi, who suggested that OPEC should allow time for existing output curbs to be felt in a world oil market where crude prices have slumped under the threat of an impending economic downturn. "This is not a good time to react quickly to what is happening in the market."

World Oil Inventories

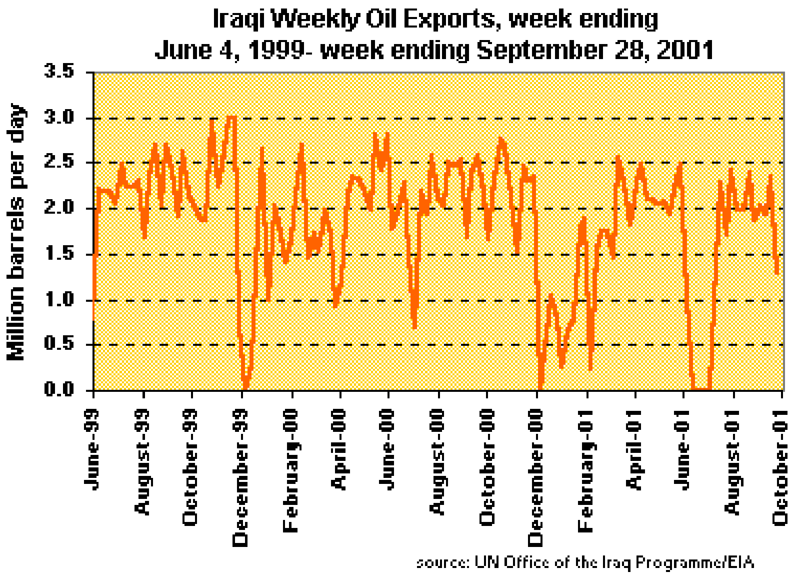
At the beginning of September, OECD commercial oil stocks were estimated to be at the bottom end of their normal range, only slightly higher than last year's extremely low levels. Prior to the crisis, the EIA Outlook indicated that unless the OPEC 10 eased off their new quotas, there was a very real possibility that these low inventories would create upward pressure on oil prices as the winter heating season approached.

With the large increase in OPEC 10 production that began during September 2001 and the decline in world oil demand, OECD commercial stocks are projected to loosen and move into the middle of their normal range in 2002. The EIA Outlook does not factor in stock-building in anticipation of a possible shortage that could occur as a result of the events of September 11, although there have been indications that some stockpiling may have occurred immediately after these events.

EIA does not attempt to estimate oil inventory levels on a global basis. However, the direction in which OECD commercial oil inventories are headed is discerned from EIA's world oil supply and demand estimates.

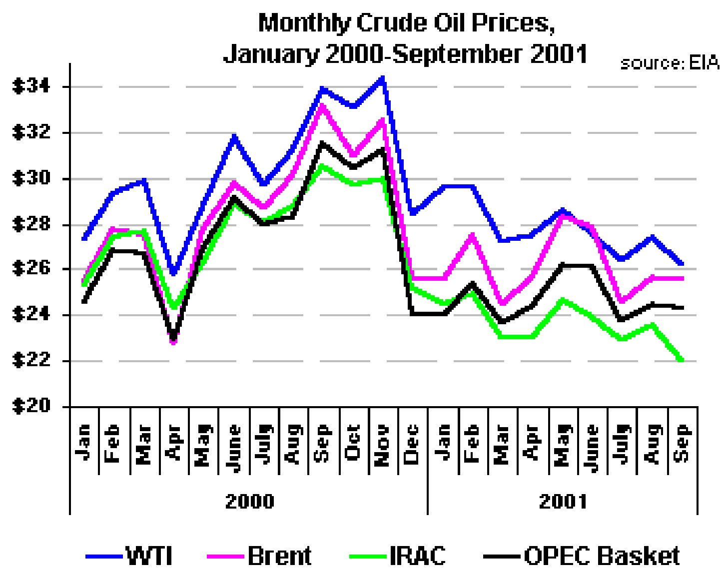
IRAQ

In September, Iraq averaged about 1.9 million bbl/d in United Nations-sanctioned oil-for-food exports. While weekly levels continue to fluctuate, exports resumed quickly after Iraq's four-week suspension in June-July. Although controversies related to pricing policies for Iraqi crude continue and Iraqi exports typically fall at the end of each phase of the UN's oil-for-food program, no other major disruptions in exports are expected in the near term.



There have been repeated pricing controversies in recent months. In an effort to illegally generate income for the regime through oil exports, Iraq often charges a "surcharge" on top of the UN-approved selling price for the crude that is outside the purview of UN supervision. Iraq has tried to sell its oil for official prices that the UN believes are below-market levels. The differential between the official price and the market price for Iraqi oil allows room for the illegal surcharge, which has been estimated by UN Security Council experts at $0.30 per barrel compared with a typical premium of $0.05 per barrel earned by traders.

The United States and the United Kingdom have asked for more frequent price analyses by in-house UN oil industry experts, alerting the UN sanctions committee when official selling prices diverge from values on the cash market. In September, the Security Council agreed to receive weekly updates on oil prices from the oil overseers. Iraq has countered that its prices should be more stable and approved no more frequently than once a month. UN Security Council members Russia and China also object to more frequent pricing reviews.



WORLD OIL PRICING

OPEC collects pricing data on a "basket" of seven crude oils, including: Algeria's Saharan Blend, Indonesia's Minas, Nigeria's Bonny Light, Saudi Arabia's Arab Light, Dubai's Fateh (or Dubai), Venezuela's Tia Juana Light, and Mexico's Isthmus (a non-OPEC crude oil). It uses the price of this basket to monitor world oil market conditions, and the basket price triggers the price band mechanism.

Major world crude oils important for oil pricing, called "benchmark" crudes, include U.S. West Texas Intermediate (WTI) and North Sea Brent crude. Because WTI is a very light, sweet (low sulfur content) crude, it is generally more expensive than the OPEC basket, which is an average of light sweet crude oils such as Algeria's Saharan Blend and heavier sour crudes (with high sulfur content) such as Dubai's Fateh. Brent is also lighter, sweeter, and more expensive than the OPEC basket, although less so than WTI. WTI generally trades at about a $2 premium to Brent.

The average price for imported oil paid by U.S. refiners is referred to as the Imported Refiners' Acquisition Cost (IRAC). This average cost for imported oil is used as a proxy for the average world oil price, and is the world oil price used in EIA's *Short-Term Energy Outlook*. The IRAC price and OPEC basket price have tracked closely during the past few years. However, in recent months, the IRAC price has tracked lower than usual. The OPEC basket has been $1+ higher than the IRAC, while WTI has been $3 higher than IRAC.

OPEC Crude Oil Production [1]
(Thousand barrels per day)

	3Q 2001 Production	4Q 2001 Production	9/01/01 Quota[2]	4Q Production Capacity[3]	4Q Surplus Capacity[3]
Algeria	825	773	741	975	202
Indonesia	1,214	1,203	1,203	1,250	47
Iran	3,733	3,571	3,406	3,900	329
Kuwait[4]	2,004	1,995	1,861	2,200	205
Libya	1,362	1,326	1,242	1,550	224
Nigeria	2,071	2,166	1,911	2,300	134
Qatar	685	654	601	735	81
Saudi Arabia[4]	8,104	8,000	7,541	10,000-10,500[5]	2,000-2,500[5]
UAE[6]	2,148	2,141	2,025	2,650	509
Venezuela	2,822	2,754	2,670	3,100	346
OPEC 10 Crude Oil Total	**24,969**	**24,583**	**23,200**	**28,660 - 29,160[5]**	**4,077 - 4,577[5]**
Iraq[7]	2,604	2,382	N/A	3,000	618

OPEC Crude Oil Total	**27,573**	**26,965**		**31,660 - 32,160[5]**	**4,695 - 5,195[5]**
Other Liquids[8]	2,771	2,771			
Total OPEC Production	**30,344**	**29,736**			

NA: Not Applicable
[1]*Crude oil does not include lease condensate or natural gas liquids.*
[2]*Quotas are based on crude oil production only.*
[3]*Maximum sustainable production capacity, defined as the maximum amount of production that: 1) could be brought online within a period of 30 days; and 2) sustained for at least 90 days.*
[4]*Kuwaiti and Saudi Arabian figures each include half of the production from the Neutral Zone between the two countries. Saudi Arabian production also includes oil produced from its offshore Abu Safa field on behalf of Bahrain.*
[5] *Saudi Arabia is the only country with the capability to further increase its capacity significantly within 90 days. Saudi Arabia can increase its sustainable production capacity to 10 million bbl/d within 30 days and to 10.5 million bbl/d within 90 days. As a result, the estimates for Saudi Arabia are as shown as a range, with the lower figure using the 30 days' definition and the upper end reflecting Saudi Arabia's 90 days' capability. OPEC's surplus capacity estimates are also shown as a range for this reason.*
[6]*The UAE is a federation of seven emirates. The quota applies only to the emirate of Abu Dhabi, which controls the vast majority of the UAE's economic and resource wealth.*
[7]*Iraqi oil exports are approved by the United Nations under the oil-for-food program for Iraq established by Security Council Resolution 986 (April 1995) and subsequent resolutions. As a result, Iraqi production and exports have not been a part of any recent OPEC agreements. Resolution 986 limited the sale of Iraqi crude oil over six-month periods to specified dollar amounts. However, the Security Council voted to remove any limits on the amount of oil Iraq could export in December 1999.*
[8]*Other liquids include lease condensate, natural gas liquids, and other liquids including volume gains from refinery processing.*

MEETINGS, ANNOUNCEMENTS, AND RELATED EVENTS

The OPEC 10 countries hold meetings at OPEC headquarters in Vienna, Austria, where they decide issues and make announcements that influence world oil markets and prices. Major decisions and announcements in 2001 include:

January 17, 2001: OPEC agreed to cut production quotas by 1.5 million bbl/d, effective February 1, 2001.

March 16, 2001: OPEC agreed to cut production quotas by 1 million bbl/d, effective April 1, 2001.

June 1, 2001: The ninth phase of the oil-for-food program concluded; the United Nations approved a 30-day rollover of the program.

June 4, 2001: Iraq halted oil-for-food exports.

June 5, 2001: OPEC held its 115th meeting to review the state of world oil markets, leaving quotas unchanged.

July 3, 2001: OPEC held its 116th meeting to discuss the impact of Iraqi oil export cuts, again leaving quotas unchanged. Also, the one-month rollover of the oil-for-food program ended, and the UN approved another five months of the program with Security Council Resolution 1360.

July 10, 2001: Iraq resumed oil-for-food exports.

July 25, 2001: OPEC agreed to cut production quotas by 1 million bbl/d, effective September 1, 2001.

September 26, 2001: OPEC held its 117thmeeting to review world oil markets, leaving production quotas unchanged.

October 5, 2001: The OPEC basket price will have remained below $22 for 10 trading days (assuming price trends as of October 2 continue until October 5), raising the possibility that the price band mechanism could be activated.

November 14, 2001: OPEC will hold its 118th meeting to review oil markets.

November 30, 2001: The current phase of Iraq's oil-for-food program will end.

BACKGROUND

The Organization of Petroleum Exporting Countries (OPEC) was founded in Baghdad, Iraq, in September 1960, to unify and coordinate members' petroleum policies. OPEC members' national oil ministers meet regularly to discuss prices and, since 1982, to set crude oil production quotas. Original OPEC members include Iran, Iraq, Kuwait, Saudi Arabia, and Venezuela. Between 1960 and 1975, the organization expanded to include Qatar (1961), Indonesia (1962), Libya (1962), the United Arab Emirates (1967), Algeria (1969), and Nigeria (1971). Ecuador and Gabon were members of OPEC, but Ecuador withdrew in December 1992, and Gabon followed suit in January 1995. EIA estimates the current eleven OPEC members account for roughly 40% of world oil production and about 77% of the world's proven oil reserves.

Links

For more information on OPEC, see these other sources on the EIA web site:
EIA Information on OPEC
Monthly Energy Chronology
Non-OPEC Fact Sheet
Persian Gulf Oil Export Fact Sheet
Short-Term Energy Outlook - International Petroleum Supply and Demand with OPEC Production

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